No. 84-261 (6)

In the Supreme Court of the United States

OCTOBER TERM, 1984

COMMODITY FUTURES TRADING COMMISSION,
PETITIONER

v.

GARY WEINTRAUB, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE COMMODITY FUTURES TRADING COMMISSION

REX E. LEE
Solicitor General

PAUL M. BATOR
Deputy Solicitor General

BRUCE N. KUHLIK
Assistant to the Solicitor General
Department of Justice
Washington, D.C. 20530
(202) 633-2217

KENNETH M. RAISLER
General Counsel

WHITNEY ADAMS
Deputy General Counsel

HELEN G. BLECHMAN
Attorney
Commodity Futures Trading Commission
Washington, D.C. 20581

49 pp

QUESTION PRESENTED

Whether the trustee of a corporation in bankruptcy has the power to waive (or assert) the debtor corporation's attorney-client privilege with respect to communications that took place before the petition in bankruptcy was filed.

PARTIES TO THE PROCEEDING

Petitioner, the Commodity Futures Trading Commission, applied to enforce an administrative subpoena in the district court and was the appellee in the court of appeals.

Respondent Gary Weintraub, a respondent in the district court, did not appeal from the district court's order.

Respondents Frank H. McGhee and Andrew McGhee intervened as respondents in the district court and were appellants in the court of appeals.

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OPINIONS BELOW

The original opinion of the court of appeals (Pet. App. 1a-11a) is unreported. An order of the court of appeals modifying that opinion (Pet. App. 12a-16a) is also unreported. The opinion of the court of appeals as modified is reported at 722 F.2d 338.

JURISDICTION

The judgment of the court of appeals (Pet. App. 23a-24a) was entered on November 21, 1983. A petition for rehearing was denied on April 18, 1984 (Pet. App. 21a-22a). On July 10, 1984, Justice Stevens extended the time within which to file a petition for a writ of certiorari to and including August 16, 1984. The petition was filed on that date and granted

on October 29, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTORY PROVISIONS INVOLVED

Pertinent portions of the Bankruptcy Reform Act of 1978, 11 U.S.C. 101 *et seq.*, are reprinted at Pet. App. 25a-36a.

STATEMENT

1. This case arises out of a formal investigation by the Commodity Futures Trading Commission (CFTC) to determine whether Chicago Discount Commodity Brokers (CDCB) or persons associated with that firm violated the antifraud or other provisions of the Commodity Exchange Act (Act), 7 U.S.C. 1 *et seq.* CDCB was a discount commodity brokerage house registered with the CFTC as a futures commission merchant pursuant to 7 U.S.C. 6d(1). On October 27, 1980, the Commission filed a complaint against CDCB in the United States District Court for the Northern District of Illinois, alleging violations of the Act.[1] The same day, Frank McGhee, acting as sole director and officer of CDCB,[2] entered into a consent decree with the CFTC providing, inter alia, for a freeze on CDCB's assets and the appointment of a receiver (R. Supp.[3] Exh. 1). In the consent

[1] *Commodity Futures Trading Commission* v. *Chicago Discount Commodity Brokers, Inc.*, 80 C 5755 (N.D. Ill.).

[2] On October 21, 1980, respondent Andrew McGhee had resigned as officer and director, and on October 22, 1980, Larry Cote had resigned his positions as Secretary and Vice-President of CDCB (Pet. App. 14a; J.A. 15-16). Respondent Frank McGhee was thus the sole remaining director and officer of CDCB as of October 22, 1980 (Pet. App. 14a; J.A. 17).

[3] "R. Supp." refers to the record supplement proposed by the CFTC and made part of the record by the court of appeals through an order dated January 6, 1984.

decree, Frank McGhee authorized the receiver to file a petition for liquidation of CDCB under Chapter 7 of the Bankruptcy Reform Act of 1978 (Bankruptcy Code). Pet. App. 2a, 14a; J.A. 17; R. Supp. Ex. 1, at 7.

On November 4, 1980, the receiver, John K. Notz, Jr., filed a voluntary petition in bankruptcy on CDCB's behalf, seeking liquidation under Subchapter IV of Chapter 7 of the Bankruptcy Code, 11 U.S.C. 761 *et seq.*[4] See Pet. App. 29a-34a. Notz was appointed interim trustee pursuant to Section 15701[5] of the Bankruptcy Code (Pet. App. 36a) and was later made the permanent trustee pursuant to Section 702 (Pet. App. 2a, 27a). When the bankruptcy petition was filed, the CFTC commenced its formal investigation pursuant to 7 U.S.C. 12(a) and 15.[6]

On January 28, 1981, the Commission served an investigatory subpoena upon CDCB's former counsel, respondent Gary Weintraub, seeking his testimony about matters including suspected fraudulent activi-

[4] *In re Chicago Discount Commodity Brokers, Inc.*, No. 80 B 14472 (Bankr. N.D. Ill. Nov. 4, 1980) Subchapter IV is the only bankruptcy avenue available to a commodity broker. 11 U.S.C. 109(d).

[5] Chapter 15 of the Code (11 U.S.C. 1501 *et seq.*) contains special provisions concerning United States trustees applicable in certain judicial districts, including the Northern District of Illinois. See 11 U.S.C. 1501(7). For purposes of this case, Section 15701 does not differ in relevant respects from Section 701.

[6] The investigation was confidential. Information obtained during its course may not be disclosed to third parties absent Commission authorization. See 17 C.F.R. 11.3. Cf. *SEC* v. *Jerry T. O'Brien, Inc.*, No. 83-751 (June 18, 1984). Certain of the documents in the record of this case were placed under seal by the district court.

ties and misappropriation of customer funds by CDCB's officers and employees. Weintraub appeared for his deposition and responded to certain inquiries, but refused to answer 23 questions on the basis of CDCB's attorney-client privilege. Pet. App. 2a-3a; J.A. 25-32. The questions that Weintraub refused to answer concerned CDCB's pre-bankruptcy affairs, including Weintraub's role in the corporation, the location of the corporation's funds, the identity of persons who deposited corporate funds in Weintraub's personal trading account, the amount of customer equity, personal loans made to corporate officers, and the corporation's policies about access to the corporate safe (*ibid.*).

2. On December 15, 1981, the Commission filed this subpoena enforcement action (pursuant to 7 U.S.C. 15) in the United States District Court for the Northern District of Illinois, to compel Weintraub to answer the questions as to which he had asserted CDCB's privilege (J.A. 33-36). After determining that waiver of the privilege would be in the best interests of the CDCB estate in light of potential claims by the estate against CDCB's former management and others,[7] the trustee in bankruptcy, on March 11, 1982, waived the corporation's attorney-client privilege with respect to any communications that occurred on or before October 27, 1980.[8] Pet. App. 3a;

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[7] See Brief of John K. Notz, Jr., Trustee, as Amicus Curiae In Support of CFTC Petition for Rehearing 1; Brief of John K. Notz, Jr., as Amicus Curiae In Support of Petition for Certiorari 2-5 (Trustee's Pet. Amicus Br.).

[8] The trustee waived CDCB's privilege in response to the Commission's written request. In its letter to the trustee (J.A. 47-48), the Commission outlined its year-long efforts to locate missing customer funds and determine the causes for CDCB's bankruptcy and its belief that the corporate

J.A. 49. On April 26, 1982, a United States magistrate granted the Commission's application for an order compelling Weintraub to answer, on the ground that the trustee had validly waived CDCB's privilege (Pet. App. at 19a-20a).[9] The district court upheld the magistrate's order on June 9, 1982 (*id.* at 18a). Frank and Andrew McGhee were granted leave to intervene on June 30, 1982 (Pet. App. 3a; J.A. 50-51),[10] and argued that the trustee's waiver was inef-

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debtor's privilege was being used to block access to relevant information regarding the debtor's assets and daily business operations. In his capacity as interim trustee for CDCB (see 11 U.S.C. 701), Notz was requested by the Commission to waive the corporation's attorney-client privilege "in the best interests of the creditors of CDCB as well as the corporate debtor" (J.A. 48). Before the CFTC's request, Notz had initiated his own investigation of the debtor's property, affairs and conduct pursuant to 11 U.S.C. 704(4). On November 17 and December 16, 1981, the trustee attempted to depose Weintraub pursuant to Federal Bankruptcy Rule 205(a), seeking information concerning the location of certain corporate property and the activities of certain persons against whom the trustee later filed adversary proceedings; Weintraub asserted the attorney-client privilege in response to Notz's questions. Trustee's Pet. Amicus Br. 3; Brief of John K. Notz, Trustee, As Amicus Curiae In Support of CFTC Petition for Rehearing, App. 1-176. At the time of the CFTC's March 1982 request, Notz had initiated and was pursuing a number of adversary actions on behalf of the CDCB estate, seeking to recover over $3 million of the estate's property that, he alleged, had been fraudulently conveyed to Frank and Andrew McGhee. See *id.* at 8-9; Trustee's Pet. Amicus Br. 5, App. A.

[9] The magistrate made no findings as to the attorney-client privilege that Weintraub had asserted on behalf of the McGhees as individuals (Pet. App. 19a-20a).

[10] The McGhees sought leave to intervene ostensibly for the purpose of asserting their personal attorney-client privi-

fective over their objection as "former management" (R. 49, at 7).[11] On July 27, 1982 the district court clarified its earlier order to provide that Weintraub must respond without asserting CDCB's attorney-client privilege[12] (Pet. App. 17a). The McGhees appealed from the July 27 order.[13]

3. The court of appeals reversed (Pet. App. 1a-16a).[14] The court concluded that a bankruptcy

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leges, asserting that Weintraub had acted as their personal attorney in traffic matters, arbitration proceedings, disciplinary proceedings brought against them by a commodity exchange and the CDCB bankruptcy proceeding. R. 42 ¶ 1, at 2. They did not argue against the trustee's authority to exercise the corporate privilege until their July 19, 1982 reply to the CFTC's response to their motion to vacate or modify the magistrate's order (R. 49, at 7).

[11] The McGhees did not argue that the trustee's waiver was contrary to the best interests of the debtor (R. 49, at 7). In this regard, it should be noted that Frank McGhee was convicted in 1983 of embezzling $3.5 million of CDCB's customer funds in violation of Section 9(a) of the Commodity Exchange Act, 7 U.S.C. 13(a), and sentenced to three years' incarceration. *United States* v. *Frank McGhee*, No. 83 Cr. 262-1 (N.D. Ill. Oct. 7, 1983).

[12] The earlier order had not explicitly limited the waiver of the attorney-client privilege to that asserted on behalf of the corporation (Pet. App. 18a).

[13] Because the district court refused to compel Weintraub to testify pending appeal (Pet. App. 4a n.4), the Commission has not yet obtained answers to the questions at issue. While administrative proceedings have already been initiated against respondents, Weintraub's answers could provide information for additional causes of action, or claims against other persons.

[14] On its own motion, the panel revised its opinion on March 19, 1984 (Pet. App. 12a-16a), but reached the same

trustee does not have the power to waive a corporate debtor's attorney-client privilege with respect to communications that occurred before the filing of the bankruptcy petition (*id.* at 11a). Although it took note of the broad powers accorded a trustee under the Bankruptcy Code, the court concluded that those powers do not include the power to waive or assert the corporate debtor's attorney-client privilege for four reasons: the trustee does not under the Code "replace the corporation * * * [or] succeed to the positions of [its] officers and directors" (*id.* at 9a); waiver by the trustee of a corporate debtor would treat such debtors less favorably than individuals in bankruptcy (*id.* at 9a-10a); waiver by the trustee would discriminate against bankrupt corporations as compared to solvent corporations (*id.* at 10a); and, "most importantly," waiver by the trustee could chill attorney-client communications (*id.* at 10a-11a).

The court of appeals recognized that its decision conflicts with *Citibank, N.A.* v. *Andros*, 666 F.2d 1192 (8th Cir. 1981), which held that the trustee of a corporation undergoing liquidation pursuant to the former Bankruptcy Act, 11 U.S.C. (1976 ed.) 110(a), could waive the debtor's attorney-client privilege, but declined to follow it (Pet. App. 15a-16a). The court also noted that *In re O.P.M. Leasing Services, Inc.*, 670 F.2d 383 (2d Cir. 1982), held that the trustee of a corporation undergoing reorganization pursuant to Chapter 11 of the Bankruptcy Code could waive the corporation's attorney-client privilege, but distinguished it on the ground that the board of directors

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result as it had earlier (*id.* at 1a-11a). The CFTC's petition for rehearing was denied without opinion (*id.* at 21a-22a). The petition had been supported by the Securities and Exchange Commission, the United States Trustee for the Northern District of Illinois, and the trustee for CDCB.

of the corporation there was no longer in existence, while here, Frank McGhee remained an officer and director (Pet. App. 14a-15a).

SUMMARY OF ARGUMENT

Control of a corporation's attorney-client privilege rests with its management. As a function of management, the power to assert or waive the corporate privilege changes when new management is installed. Management's decision to waive or exercise the privilege may not be overruled by individual officers or directors, even with respect to their own communications with corporate counsel.

In the case of a corporate debtor in bankruptcy, it is the trustee who constitutes the management. The trustee represents the estate, is vested with all legal and equitable interests of the debtor, and is authorized to operate its business. The trustee, as an arm of the bankruptcy court, owes a fiduciary duty to all parties in interest, including the corporation's equity holders, to maximize the value of the assets of the estate. The debtor's officers and directors are ousted of all management functions in favor of the trustee.

As the person managing the debtor under the Bankruptcy Code, the trustee is the proper party to assert or waive its attorney-client privilege. Control over the privilege is a necessary incident of the trustee's powers over the debtor's affairs and his duties to interested parties. Corporate bankruptcies are not infrequently associated with possible misconduct on the part of former management; this is particularly true in the case of commodity broker bankruptcies. Causes of action against officers and directors for the losses caused by their misconduct are assets of the estate. Because former corporate counsel may be the best or even the only source of information regarding these

causes of action, it is essential that the trustee have control over the corporation's privilege.

Like the management of a solvent corporation, the bankruptcy trustee may conclude that the corporation's interests would best be served by cooperating with government investigations into the conduct of individual officers and directors. Such cooperation is especially useful in bankruptcy, where the estate's limited assets may make effective investigation by the trustee alone difficult or impossible. When the trustee, acting in the best interests of the estate, elects to waive the attorney-client privilege, he is not acting as a prosecutor or similar entity foreign to the corporation any more than is management of a corporation not in bankruptcy when it waives the privilege. The policy concerns expressed by the court of appeals fail to take account of the operation of the corporate attorney-client privilege outside bankruptcy or of the trustee's role in bankruptcy. Permitting pre-bankruptcy officers and directors to veto the trustee's decisions would allow them to use the privilege to shield their own wrongdoing. Only the trustee, supervised by the court, can be relied upon to act in the best interests of all concerned.

ARGUMENT

THE TRUSTEE OF A CORPORATION IN BANKRUPTCY HAS THE POWER TO ASSERT OR WAIVE THE CORPORATION'S ATTORNEY-CLIENT PRIVILEGE WITH RESPECT TO COMMUNICATIONS THAT TOOK PLACE BEFORE THE PETITION IN BANKRUPTCY WAS FILED

A. Control Of A Corporation's Attorney-Client Privilege Is A Function Of Its Management

The question raised by this case is: who is the proper party to act for a corporation in asserting or waiving *the corporation's* attorney-client privilege

when it is undergoing liquidation pursuant to Chapter 7 of the Bankruptcy Code.[15] A corporation, as an artificial entity, must of course act through persons. It is settled that the power to assert or waive a corporation's attorney-client privilege rests with its management—normally the board of directors—or those authorized by management to assert this power.[16] See, *e.g.*, *In re O.P.M. Leasing Services, Inc.*, 670 F.2d 383, 386 (2d Cir. 1982); *Citibank, N.A.* v. *Andros*, 666 F.2d 1192, 1195 (8th Cir. 1981); *In re Grand Jury Investigation*, 599 F.2d 1224, 1236 (3d Cir. 1979); *Stewart Equipment Co.* v. *Gallo*, 32 N.J. Super. 15, 107 A.2d 527 (Law Div. 1954); Note, *The Lawyer-Client Privilege: Its Application to Corporations, the Role of Ethics, and Its Possible Curtailment*, 56 Nw. U. L. Rev. 235, 243-244 (1961); see also *United States* v. *De Lillo*, 448 F. Supp. 840 (E.D.N.Y. 1978) (board of trustees of pension fund is proper entity to waive privilege, by analogy to corporations); cf. *Garner* v. *Wolfinbarger*, 430 F.2d

[15] The same principles apply, and the same result should obtain, with respect to the trustee of a corporation undergoing reorganization pursuant to Chapter 11. See note 42, *infra*.

[16] State corporation laws generally vest management authority in a corporation's board of directors. *E.g.*, Del. Code Ann. tit. vii, § 141 (1976); N.Y. Bus. Corp. Law § 701 (McKinney Supp. 1983-1984); Ill. Ann. Stat. ch. 32, § 8.05 (Smith-Hurd Supp. 1984-1985). See Model Bus. Corp. Act § 35 (1979). In practice, a large corporation is typically managed by its top officers, but their authority legally derives from that of the board of directors. See Eisenberg, *Legal Models of Management Structure in the Modern Corporation: Officers, Directors, and Accountants*, 63 Calif. L. Rev. 375 (1975). The distinctions generally drawn between officers and directors are not relevant to the question presented in this case.

1093, 1103-1104 (5th Cir. 1970), cert. denied, 401 U.S. 974 (1971) (in derivative action, shareholders may for good cause overcome management's assertion of the privilege). Management's decisions with respect to the privilege, as in all other matters, must be consistent with its fiduciary duty to act in the best interests of the corporation. See generally, *e.g.*, *Dodge* v. *Ford Motor Co.*, 204 Mich. 459, 507, 170 N.W. 668, 684 (1919).

It is also settled that a corporation's privilege may not be asserted by individual directors or officers in their own right. Indeed, a corporation may, over the objection of a director or officer, waive its privilege with respect to his communications to the corporation's attorney. When control of a corporation or similar entity passes to new management, control over the attorney-client privilege passes as well. Accordingly, it is clear that when new management is installed as a result of a takeover, merger, change in shareholder composition, or other business development, the new managers may waive the attorney-client privilege with respect to communications made by former officers and directors. See, *e.g.*, *United States* v. *Bartlett*, 449 F.2d 700, 704 (8th Cir. 1971), cert. denied, 405 U.S. 932 (1972) (chief executive officer); *United States* v. *Piccini*, 412 F.2d 591, 593 (2d Cir. 1969), cert. denied, 397 U.S. 917 (1970) (officer and shareholder); *United States* v. *De Lillo*, 448 F. Supp. at 842; *In re Grand Jury Proceedings*, 434 F. Supp. 648 (E.D. Mich. 1977), aff'd per curiam, 570 F.2d 562 (6th Cir. 1978) (vice-president); *In re Grand Jury Subpoena Duces Tecum*, 391 F. Supp. 1029, 1034 (S.D.N.Y. 1975) (president and chairman of the board); *United States* v. *Koenig*, [1973-1974 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,413 (sum-

mary) (S.D.N.Y. 1974) (president); *In re Crescent Beach Inn, Inc.*, 40 Bankr. 56 (Bankr. Me. 1984).[17]

B. The Trustee Of A Corporate Debtor Succeeds To Its Management Functions

1. When a trustee is appointed in a corporate bankruptcy,[18] management's powers and duties pass

[17] Cf. *Bellis* v. *United States*, 417 U.S. 85 (1974) (partner may not assert his Fifth Amendment privilege over partnership records he holds in a representative capacity); *Joy* v. *North*, 692 F.2d 880, 893 (2d Cir. 1982), cert. denied, 460 U.S. 1051 (1983) (waiver of attorney-client privilege with respect to communications underlying special litigation report used to seek dismissal of shareholder derivative action). See generally *Diversified Industries, Inc.* v. *Meredith*, 572 F.2d 596, 611 n.5 (8th Cir. 1978) (en banc); Simon, *The Attorney-Client Privilege as Applied to Corporations*, 65 Yale L.J. 953, 988 (1956); Note, *The Attorney-Client Privilege: A Look at Its Effect on the Corporate Client and the Corporate Executive*, 55 Ind. L.J. 407, 411 (1980).

This rule comports with, although it is broader than and independent of, the principle that the privilege passes to the client's successor in interest. Cf. *NLRB* v. *Bildisco & Bildisco*, No. 82-818 (Feb. 22, 1984), slip op. 13 (debtor in possession is same entity as existed before, but with different powers and duties under the Code than it possessed outside bankruptcy). For example, when a person conveys an interest in property, the grantee receives control over the attorney-client privilege to the extent necessary to realize the granted interest. See, *e.g.*, *Walton* v. *Van Camp*, 283 S.W.2d 493 (Mo. Sup. Ct. 1955); *Buuck* v. *Kruckeberg*, 121 Ind. App. 262, 95 N.E.2d 304 (Ind. Ct. App. 1950); 8 *Wigmore on Evidence* § 2328 (McNaughton rev. 1961).

[18] Corporate business entities are limited to liquidation under Chapter 7, in which a trustee is always appointed (see 11 U.S.C. 701), or reorganization under Chapter 11, in which a trustee may be appointed only in specified circumstances, including fraud by current management (see 11 U.S.C. 1104). Stockbrokers and commodity brokers are limited to Chapter

to the trustee.[19] All corporate property passes to the estate created at the commencement of the case (see 11 U.S.C. 541).[20] "[N]o interests in property of the

7 liquidation. See 11 U.S.C. 109(d); page 19 & note 30, *infra*. (Chapter 11, which consolidates and substantially reframes Chapters X, XI, and XII of the former Bankruptcy Act, contemplates that most reorganizations will be conducted without a trustee, *i.e.*, that the debtor's management will retain control of its business to the same extent as would a trustee. See 11 U.S.C. 1107(a). In a Chapter 13 proceeding, which is designed for individuals and sole proprietorships, the trustee does not operate the debtor's business, and management remains the responsibility of the debtor. 11 U.S.C. 1304(b)). See H.R. Rep. 95-595, 95th Cong., 1st Sess. 118-119 (1977) (House Report).

[19] With respect to the disposition of property, the trustee is supervised more closely by the bankruptcy court than is management of a solvent corporation by its shareholders. See 11 U.S.C. 363(b). Court supervision is intended to ensure that the trustee act in the best interests of the estate; it does not suggest that former management retains control over the debtor's privilege. See Note, *Waiver of the Attorney-Client Privilege by the Trustee in Bankruptcy* (Chicago Note) 23 (forthcoming 51 U. Chi. L. Rev.; a copy of this Note has been provided to the respondents and lodged with the Clerk). Indeed, the availability of such supervision suggests precisely the opposite.

[20] The estate includes "all legal or equitable interests of the debtor in property [with certain enumerated exceptions] as of the commencement of the case" (11 U.S.C. 541(a)(1)). See 4 *Collier on Bankruptcy* ¶ 541.10[8], at 541-67 (15th ed. 1984); House Report 176. The scope of the estate under Section 541 is extremely broad. See House Report 367-369; S. Rep. 95-989, 95th Cong., 2d Sess. 82-83 (1978) (Senate Report). A corporate debtor, unlike individual debtors, may not exclude any of its property from the estate. See 11 U.S.C. 522(b); 3 *Collier on Bankruptcy* ¶ 522.05[3]; cf. *In re SA Auto-Jack, Inc.*, 380 F. Supp. 99, 100 (N.D. Cal. 1974).

estate remain in the debtor." H.R. Rep. 95-595, 95th Cong., 1st Sess. 368 (1977) (House Report). The trustee is the legal representative of the estate (11 U.S.C. 323(a)) and as such succeeds to all causes of action and defenses of the corporation (11 U.S.C. 323(b) and 541).[21] The debtor is required to "surrender to the trustee all property of the estate and any recorded information * * * relating to property of the estate" (11 U.S.C. 521(3)). The trustee is "accountable for all property received" (11 U.S.C. 704(2), 1106(a)(1)). He is directed to investigate the debtor's financial affairs (11 U.S.C. 704(4), 1106(a)(3)). A significant part of this investigation is the trustee's inquiry into the actions of former management:

> One of the most important purposes of an investigation by a trustee is to inquire into the conduct, character and quality of the debtor's management and its associates, to reveal causes of action, if any, against officers, directors or others which might inure to the estate.

See 4 *Collier on Bankruptcy* ¶ 704.07, at 704-17 to 704-18 (15th ed. 1984). The trustee is specifically empowered to sue officers, directors and other insiders to recover fraudulent or preferential transfers of the debtor's property (11 U.S.C. 547(b)(4)(B), 548).[22] His ability to obtain information re-

[21] The trustee has the power to prosecute actions on behalf of the estate without prior court approval. Bankr. R. 6009. See generally *Meyer* v. *Fleming*, 327 U.S. 161, 168 (1946).

[22] The capacity to sue and defend in the name of the corporate debtor, a power only the trustee holds (11 U.S.C. 323, 541), is exclusively a management power. *Sterling Industries, Inc.* v. *Ball Bearing Pen Corp.*, 298 N.Y. 483, 84 N.E.2d 790 (1949). See *United Copper Securities Co.* v. *Amalgamated Copper Co.*, 244 U.S. 261, 263-264 (1917).

The trustee's succession to control over the corporate debtor's property gives him other management powers as well. *Great Western Tel. Co.* v. *Purdy*, 162 U.S. 329, 336 (1896); *In re Newfoundland Syndicate*, 201 F. 917 (3d Cir. 1913) (trustee succeeds to directors' right to make assessments on unpaid shares of the corporation); *In re Pipe Line Oil Co.*, 289 F. 698, 700-701 (6th Cir. 1923) (trustee holds right to enforce liability under state statutes where watered stock has been issued even though no asset was transferred); *Moore* v. *Herrink*, 77 F.2d 96, 97 (4th Cir. 1935) (trustee succeeds to the right of the corporation to treat action of the corporation's board of directors in authorizing a promissory note issued by disqualified directors as a nullity); *Hooper* v. *Mountain States Securities Corp.*, 282 F.2d 195, 206-207 (5th Cir. 1960), cert. denied, 365 U.S. 814 (1961) (trustee has standing to maintain an action for fraud on the corporation in the sale of its own securities).

garding fraudulent or other invalid transactions of the bankrupt's officers and employees is a necessary adjunct of the trustee's statutory duty to facilitate an equitable distribution of the bankrupt's assets. The trustee must therefore be afforded wide latitude in obtaining information regarding the bankrupt's property and financial affairs. *In re Browy*, 527 F.2d 799, 802 (7th Cir. 1976).[23]

When a trustee has been appointed in reorganization, he is empowered to "operate the debtor's busi-

[23] When a debtor undergoing reorganization remains in possession, the investigative function may be carried out by an examiner (11 U.S.C. 1106(b)). See House Report 234 (explaining that appointment of an examiner may be appropriate to provide for an investigation of former management's wrongdoing while permitting new management, rather than a trustee, to operate the business as a debtor in possession).

ness" unless the court orders otherwise (11 U.S.C. 1108). Even in liquidation, where the trustee is directed to reduce the property of the estate to money and "close up [the] estate as expeditiously as is compatible with the best interests of parties in interest" (11 U.S.C. 704(1)), the court "may authorize the trustee to operate the business" (11 U.S.C. 721) if continued operation of the debtor's business for a limited time is desirable. House Report 220-221.[24] The trustee is also authorized by the Code to enter into transactions in the course of operating the debtor's business (11 U.S.C. 363(b) and (c)(1)).[25]

The bankruptcy trustee's fiduciary responsibilities parallel those imposed on the management of a solvent corporation. The trustee has a duty to maximize the value of the estate. 11 U.S.C. 323, 704(1); see, *e.g.*, *In re Washington Group, Inc.*, 476 F. Supp. 246,

[24] When operating the debtor's business under either Chapter 7 or Chapter 11, the trustee may, when authorized by the court, employ professional persons, including accountants and attorneys, to represent or assist him in carrying out his duties (11 U.S.C. 327(a) and (b)). Upon court approval, the trustee may also employ "for a specified special purpose * * * an attorney that has represented the debtor, if in the best interest of the estate, and if such attorney does not represent or hold any interest adverse to the debtor or to the estate with respect to the matter on which such attorney is to be employed" (11 U.S.C. 327(e)). It would be incongruous to empower the trustee to retain the debtor's counsel while withholding control over the attorney-client privilege.

[25] Section 363(c)(1) provides that the trustee may enter into transactions "in the ordinary course of business" without prior approval by the court, but Section 363(b) requires such approval for the "use, [sale], or lease, other than in the ordinary course of business, [of] property of the estate." See also note 19, *supra*.

250 (M.D.N.C. 1979), aff'd *sub nom. Johnston* v. *Gilbert*, 636 F.2d 1213 (4th Cir. 1980), cert. denied, 452 U.S. 940 (1981). This duty runs not simply to the debtor's creditors, but to all claimants with an interest in the estate, including the corporation's equity holders.[26] See, *e.g.*, *B & L Farms Co.* v. *United States*, 238 F. Supp. 407, 410 (S.D.Fla. 1964), aff'd, 368 F.2d 571 (5th Cir. 1966), cert. denied, 389 U.S. 835 (1967) ("bankruptcy trustees do not represent the creditors alone[;] [t]hey must protect the interests of the bankrupt"); *In re Ducker*, 134 F. 43, 47 (6th Cir. 1905); Baird & Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51 U. Chi. L. Rev. 97, 101-109 (1984). See generally *Wolf* v. *Weinstein*, 372 U.S. 633, 649-651 (1963). When the trustee acts to maximize the value of the estate, he acts in the best interests of the debtor's shareholders, who have a claim to any surplus remaining after the distribution of assets to creditors. See generally 11 U.S.C. 507. For these reasons, the trustee's fiduciary duties are analogous to those of the management of a corporation not in bankruptcy. See Note, *Waiver of the Attorney-Client Privilege by the Trustee in Bankruptcy* (Chicago Note) 21 (forthcoming 51 U. Chi. L. Rev.).[27]

[26] Similarly, the management of an insolvent corporation not in bankruptcy owes a duty not just to the equity holders, but to creditors as well. See generally *McCandless* v. *Furlaud*, 296 U.S. 140, 156-157 (1935). The trustee of a corporation in bankruptcy stands in the same position as the corporation's directors when they are permitted to remain in possession: both owe fiduciary obligations to the entire estate, including creditors. See 11 U.S.C. 1107; *Wolf* v. *Weinstein*, 372 U.S. 633, 643, 649 (1963).

[27] See note 19, *supra*.

In sum, a bankruptcy trustee is granted substantially complete management authority over the debtor.[28] See 2 *Collier on Bankruptcy* ¶ 323.01, at 323-2 (15th ed. 1984); 4 *id.* ¶¶ 760.01 *et seq.* Former management's role is limited to turning over the corporation's property to the trustee and to providing certain information to the trustee and creditors (11 U.S.C. 521, 343). Congress contemplated that when a trustee has been appointed, he must be put in control of the business and former management "completely ousted." House Report 220-221.[29]

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[28] The court of appeals' failure to recognize this may be attributable to its confusion of various provisions of the Bankruptcy Code. The court relied almost exclusively on 15A W. Fletcher, *Cyclopedia of the Law of Private Corporations* § 7657 (rev. ed. 1981), in concluding that a corporation "is capable of numerous functions even after the filing of the petition in bankruptcy" (Pet. App. 9a). The cited section of Fletcher's treatise, however, does not deal with the question of who, under present law, has the power to manage a bankrupt entity once a trustee has been appointed. Moreover, the court ignored the importance of the special provisions governing commodity brokers, which completely divest former management of any control over the firm's operations (see pages 19-21, *infra*).

[29] See also House Report 104 (the trustee assumes the "management of the debtor's property and the operation of the debtor's business"); 11 U.S.C. 1105 (trustee's appointment may be terminated by the court and the debtor *restored* "to possession and *management* of the property of the estate, and operation of the debtor's business") (emphasis added). Cf. *Wolf* v. *Weinstein*, 372 U.S. at 651; *Great Western Tel. Co.* v. *Purdy*, 162 U.S. at 336; *Weck* v. *District Court*, 161 Colo. 384, 422 P.2d 46 (1967) (trustee takes the place of and exercises the office of the directors). While these references are to the role of the trustee in reorganization, nothing in the Code or its legislative history suggests that Congress contemplated that a trustee in managing a liquidation would have any less control over the affairs of the debtor. See note 42, *infra*.

2. The trustee's role as manager of the corporate debtor emerges with special clarity in the provisions of the Code (Subchapter IV of Chapter 7) governing commodity broker bankruptcies.[30] These provisions were derived largely from proposals by the Commission and reflect Congress's recognition that special legislation was essential to address the complex problems raised by the liquidation of commodity businesses and to prevent commodity broker bankruptcies from having a "ripple effect" that could threaten the integrity of commodity futures markets. House Report 271-272. See generally *Merrill Lynch, Pierce, Fenner & Smith* v. *Curran*, 456 U.S. 353, 357-367 (1982). To protect futures markets,[31] as well as the

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[30] 11 U.S.C. 761-766. Commodity broker bankruptcies may proceed only under Chapter 7 (11 U.S.C. 109(d)) because Congress determined that the special protections it intended to afford commodity customers would not be available in Chapter 11. House Report 319. Like commodity brokers, stockbrokers may not utilize Chapter 11. Rather, they are liquidated either under Subchapter III of Chapter 7 (11 U.S.C. 741 *et seq.*) or, as is most often the case, under the Securities Investors Protection Act of 1970 (SIPA), 15 U.S.C. 78aaa *et seq.* Trustees appointed under SIPA have the same general managerial responsibilities as bankruptcy trustees appointed in commodity broker liquidations. See 15 U.S.C. 78fff-1.

[31] Protection of market stability during a commodity broker insolvency is more difficult in the commodities markets than in other markets. Commodity futures, options, and leverage contracts all have limited duration. In addition, gains and losses on open positions in the futures markets are paid out on a daily basis through variation margin payments. Thus, the trustee of an insolvent commodity broker does not have the luxury of an extended period within which to analyze the debtor's business and determine the best course of action. Delay by the trustee can result in default in making the daily variation margin

customers of insolvent commodity brokers,[32] the Commission was given rulemaking authority, which it has exercised, to regulate the conduct of the debtor's business and its liquidation. 7 U.S.C. 24; 17 C.F.R. Pt. 190; see S. Rep. 95-989, 95th Cong., 2d Sess. 8 (1978) (Senate Report).

Under the statutory and regulatory provisions governing the operation of a bankrupt commodity broker, the firm's officers and directors play no role. Beginning on the day of the order for relief,[33] the trustee is responsible for all management functions, including assessing the shortfall in customer funds,

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payments, or default on delivery, either of which could have a ripple effect that disrupts the entire market. Further, abrupt actions by the trustee could seriously disrupt orderly trading, resulting in substantial losses to the bankrupt, its customers, and other market participants.

Senate Report 8; see also House Report 272.

[32] Congress intended to afford special protection to commodity customers, who, like bank trust depositors, own the funds held with the broker and thus most of the funds at risk in such a firm's bankruptcy. House Report 271-272; Senate Report 9 (commodity customers receive "the highest priority against the bankrupt's estate); see 7 U.S.C. 6d(2); 17 C.F.R. 32.6. The Commission has estimated that more than 90 percent of all claims, both in number and value, against an estate in a commodity broker bankruptcy are customer claims. Statement of Philip Johnson, Chairman, Commodity Futures Trading Commission, before the Subcomm. on Monopolies and Commercial Law of the House Comm. on the Judiciary 8-13 (July 2, 1981). As of 1980, the average amount of customer-owned funds held by each commodity broker registered as a futures commission merchant was $8.7 million. 46 Fed. Reg. 62864 (1981).

[33] The Commission's rules define "Order for Relief" as the filing of a voluntary bankruptcy petition or the adjudication of bankruptcy in an involuntary case. 17 C.F.R. 190.01(dd).

identifying open commodity contracts that are eligible for transfer, liquidating certain contracts,[34] offsetting those that otherwise would result in deliveries, and making and meeting necessary margin calls. Thereafter, the trustee must, among other things, seek instructions from customers regarding the handling of their accounts, as well as continue to carry out other necessary functions attendant to managing a commodity brokerage house.[35] The trustee must also comply with all provisions of the Commodity Exchange Act and Commission regulations "as if [he] were the debtor." 17 C.F.R. 190.04(a).[36] He owes a fiduciary duty to the firm's customers just as do officers of a commodity broker not in bankruptcy.[37] In all respects, it is the trustee who now manages the debtor corporation.

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[34] If the debtor holds an unusually large position on one side of the market, the trustee may have to extend liquidation over time to avoid market disruption. See, *e.g.*, 17 C.F.R. 190.04(d)(2).

[35] 17 C.F.R. 190.02(b)(2), 190.05. See 17 C.F.R. 190.02(g) (making margin payments and calls); 190.03(a) (operating open accounts); 190.04(b) (computing funded balances for open accounts).

[36] The trustee performs virtually identical functions to those required of any commodity broker out of compliance with the Commission's minimum financial requirements (17 C.F.R. 1.17). Under Commission Rule 1.17(a)(4), such a broker must transfer or liquidate all customer accounts and cease doing business as a broker until the firm is able to demonstrate financial compliance.

[37] See House Report 270; *Gordon* v. *Shearson Hayden Stone, Inc.*, [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,016, at 23,976 n.16 (1980), aff'd mem. *sub nom. Shearson Loeb Rhoades, Inc.* v. *CFTC*, 673 F.2d 1339 (9th Cir. 1982); *In re Rosenbaum Grain Corp.*, 103 F.2d 656, 661 (7th Cir. 1939).

C. In View Of His Powers And Responsibilities Under The Bankruptcy Code, The Trustee Is The Proper Party To Control The Debtor's Attorney-Client Privilege

The question in this case requires a determination of who, for purposes of assertion or waiver of the corporation's privilege, constitutes the "management" of a corporate debtor in bankruptcy.[38] The issue is not, as the court below suggested (Pet. App. 9a), whether the trustee technically "replace[s] the corporation as an entity" or "succeed[s] to the positions of [its] officers and directors." The question is, rather, who manages the affairs of a corporation in bankruptcy.[39] And the answer is plain: it is the

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[38] Alternatively, the Court could conclude that the trustee may assert or waive the attorney-client privilege because the power to do so is an intangible asset that passes to the trustee under the Bankruptcy Code (11 U.S.C. 521(3), 541, 542, 704). See *Citibank*, 666 F.2d at 1195; *O.P.M. Leasing*, 670 F.2d at 386 n.2; *In re Amjoe, Inc.*, 11 Collier Bankr. Cas. 2d (MB) 45 (M.D. Fla. 1976). Cf. *Ex parte Fuller*, 262 U.S. 91 (1923) (trustee has the authority to disclose the books of a bankrupt partnership over the partners' claims of privilege).

[39] See *In re Boileau*, 736 F.2d 503, 506 (9th Cir. 1984) (although nominally a debtor in possession, a sole director did not control the corporate privilege because by stipulation he had been removed from substantial participation in management of the debtor corporation); cf. *Wolf* v. *Weinstein*, 372 U.S. at 645 (individual's actual function rather than his title is controlling in bankruptcy). The legislative history of the Bankruptcy Code indicates that Congress left the privilege issue to be determined by the courts. See 124 Cong. Rec. 32400 (1978) (remarks of Rep. Edwards); *id.* at 33999 (remarks of Sen. DeConcini). See *Citibank*, 666 F.2d at 1195 n.6. See also Proposed Fed. R. Evid. 503(c), 56 F.R.D. 183, 236 (1972) ("[t]he privilege may be claimed by the * * * trustee, or similar representative of a corporation"). Although the

trustee who exercises all the management powers and responsibilities of the corporate debtor and who must therefore control its attorney-client privilege.[40] The

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Proposed Federal Rules of Evidence were never adopted by Congress, they remain standards that have been cited as authoritative sources of federal common law. *United States* v. *De Lillo*, 448 F. Supp. at 842; *In re Grand Jury Proceedings*, 434 F. Supp. at 650 n.1; 2 Weinstein *Evidence* ¶ 503(c)[01], at 503-66 to 503-68 (1980). See *Trammel* v. *United States*, 445 U.S. 40, 47 (1980) (Congress rejected the proposed rules not on their merits but to leave development of the law of privilege to judicial interpretation). Proposed Rule 503(c), as a source of federal common law, contemplates that the trustee acquires the power to assert or waive the corporation's privilege. *Citibank*, 666 F.2d at 1195; *In re O.P.M. Leasing Services*, 13 Bankr. at 60.

We note that this case does not raise the question of who has the authority to waive an *individual's* attorney-client privilege when he is in bankruptcy. Different considerations arguably may apply to such a situation. See Chicago Note 29-31.

[40] This conclusion is reinforced by the Court's decision in *Butner* v. *United States*, 440 U.S. 48 (1979). See Chicago Note 12-17. In *Butner*, the Court held that the right to rents accruing during the pendency of a bankruptcy proceeding, a question not addressed by the Code itself, should be determined by reference to state law as it applied outside the bankruptcy context. The Court stated:

> Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving "a windfall merely by reason of the happenstance of bankruptcy."

Id. at 55, quoting *Lewis* v. *Manufacturers National Bank*, 364 U.S. 603, 609 (1961). Vesting authority over the attorney-

overwhelming weight of authority agrees that the trustee managing a corporate bankrupt controls the debtor corporation's attorney-client privilege.[41]

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client privilege in the trustee comports with the general rule that the management of a corporation controls its privilege. It also serves the purpose of discouraging forum shopping and preventing arbitrary windfalls: if the management of a failing company could halt effective inquiry into its own misconduct by placing the corporation in bankruptcy and thereby retaining control of the privilege, this would provide a substantial incentive to opt for bankruptcy in order to avoid the possibility that newly installed management outside of bankruptcy might waive the privilege. Chicago Note 14-15.

[41] *In re Boileau*, 736 F.2d at 506; *In re O.P.M. Leasing Services, Inc.*, 670 F.2d 383 (2d Cir. 1982) (reorganization); *Citibank*, 666 F.2d 1195-1196 (liquidation); *Schaeffer* v. *Maxwell Energy Equip. Co.*, No. 82-JM-393 (D. Colo. Oct. 10, 1984); *Fulk* v. *Bagley*, No. C-78-333-WS (M.D.N.C. Dec. 21, 1983), reconsideration denied (Jan. 3, 1984) (Chapter X reorganization under former Bankruptcy Act); *In re Continental Mortgage Investors*, No. 76-593-S (D. Mass. July 31, 1979) (Chapter X reorganization); *In re Investment Bankers, Inc.*, 30 Bankr. 883, 886 (Bankr. D. Colo. 1983) (liquidation under Securities Investor Protection Act); *In re Nat'l Trade Corp.*, 28 Bankr. 872, 874 (Bankr. N.D. Ill. 1983) (reorganization); *In re Featherworks Corp.*, 25 Bankr. 634, 643 (Bankr. E.D. N.Y. 1982), aff'd, 36 Bankr. 460 (E.D.N.Y. 1984); *In re Smith*, 24 Bankr. 3 (Bankr. S.D. Fla. 1982) (liquidatoin); *In re Silvio De Lindegg Ocean Developments, Inc.*, 27 Bankr. 28 (Bankr. S.D. Fla. 1982) (liquidation); *In re Kaleidoscope, Inc.*, 15 Bankr. 232, 239-240 (Bankr. N.D. Ga. 1981), rev'd on other grounds, 25 Bankr. 729 (N.D. Ga. 1982) (Chapter X reorganization); *In re Amjoe, Inc.*, 11 Collier Bankr. Cas. (MB) 45 (Bankr. M.D. Fla. 1976); *Weck* v. *District Court*, 161 Colo. 384, 422 P.2d 46 (1967) (statutory accountant-client privilege). See S. Stone & R. Liebman, *Testimonial Privileges* § 1.19, at 35 & n.152 (1983) ("authorities are in accord that successors or trustees of bankrupt or dissolved corporations

On the other hand, officers and directors of a debtor corporation undergoing liquidation have been deprived of the authority to manage; there is no reason why they should be deemed to continue to possess the authority to act for the corporation with respect to its privilege.[42] If such officers and directors object to a waiver of the privilege, it is solely as individuals. Such objections are ineffective even with respect to their own communications. See pages 11-12, *supra*.

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may assert or waive the privilege"). But see *In re Vantage Petroleum Corp.*, 40 Bankr. 34, 39 (Bankr. E.D.N.Y. 1984) (reorganization); *Ross* v. *Popper*, 9 Bankr. 485 (S.D.N.Y. 1980) (Magis.) (dictum).

[42] A trustee appointed under Chapter 11 should have the power to waive or assert the debtor corporation's attorney-client privilege for reasons identical to those under Chapter 7. See Chicago Note 5-6 n.17. See generally 11 U.S.C. 323, 1106, 1108; 5 *Collier on Bankruptcy*, *supra*, at ¶ 1106.01. By virtue of Section 1106(a)(1), a reorganization trustee is vested with many of the same duties, rights and powers as a liquidation trustee. Under Section 1106(a)(3), a reorganization trustee has the same investigative and reporting responsibilities as does a liquidation trustee under Section 704(4). The only differences between the functions of the trustees arise from the different purposes of the liquidation and reorganization provisions of the Act. Because the goal of reorganization is to keep a going concern in business, a reorganization trustee has more functions associated with the operation of the corporation. Cf. *NLRB* v. *Bildisco & Bildisco*, slip op. 14. But a liquidation trustee is also empowered to operate the bankrupt's business as the court permits (11 U.S.C. 721) and must perform all other duties that would normally be performed by management seeking to recover and maximize the property of the estate for ultimate distribution to creditors and equity security holders. In a commodity broker liquidation, the trustee always has the duty to manage the firm's business. See pages 19-21, *supra*.

There is nothing in the Bankruptcy Code itself or in any other federal law that would suggest a different result. Cf. *NLRB* v. *Bildisco & Bildisco*, No. 82-818 (Feb. 22, 1984), slip op. 8-12 (special nature of collective bargaining agreements under federal law requires their somewhat different treatment in bankruptcy proceedings). To the contrary, the trustee cannot carry out his responsibilities under the Code without access to and control over the corporation's pre-petition communications with counsel. The attorney of a bankrupt corporation is often the best (and sometimes the only) repository of information about the corporation's prior affairs. If trustees cannot control access to this information they will be deprived of a vital tool necessary for effective management of the debtor's business. Because commodity broker bankruptcies are frequently associated with inadequate records (as well as allegations of insider fraud)[43], as in this case,[44] the trustee must have ac-

[43] See, *e.g.*, *In re Premex, Inc.*, No. 84-2734 (Bankr. S.D. Cal. filed June 22, 1984); *In re Auric Equities Corp.*, No. 80-13-10238 (Bankr. S.D.N.Y. filed Feb. 27, 1980); *In re Alan Abrahams & Lloyd Carr & Co.*, No. 78-204-2 (Bankr. D. Mass. filed Feb. 1, 1978). See also *In re Group J. David, Inc.* and *In re J. David Dominelli*, No. 84-00633/634-P-INV-7 (Bankr. S.D. Cal. filed Feb. 13, 1984); *In re J. David Securities*, No. 84-01309-LM7 (Bankr. S.D. Cal. filed Mar. 22, 1984); *In re Financial Partners, Ltd.*, No. 82-B-14-353 (Bankr. N.D. Ill. filed Oct. 22, 1982); *In the Matter of T&D Management Co.*, No. 81-02568 (Bankr. D. Utah filed Aug. 10, 1981); *In re Trending Cycles for Commodities, Inc.*, No. 80-00099-BKC-TCB (Bankr. S.D. Fla. filed Jan. 31, 1980) (fraud); *In re Incomco, Inc.*, No. 80 13 11217 (Bankr. S.D.N.Y. filed Aug. 1, 1980) (records).

[44] See notes 8, 11, *supra*; *In re Frank McGhee, et al.*, CFTC Docket No. 83-4.

cess to other sources of information if he is to be able to operate the debtor's business.[45] In other corporate bankruptcies, including those supervised by United States Trustees (see 11 U.S.C. 1501 *et seq.*), trustees also are regularly confronted with inadequate or missing records coupled with allegations of fraud or preferential dealings by corporate officers, making fulfillment of their duties impossible without access to pre-petition communications with counsel. Accordingly, vesting control of the debtor's attorney-client privilege in anyone other than the trustee—and especially in former management (see pages 28-30, *infra*)—would be inconsistent with the scheme established by Congress in the Bankruptcy Code.

D. The Trustee's Control Over A Debtor Corporation's Attorney-Client Privilege Is Necessary To Facilitate The Discovery And Redress Of Fraud And Other Misconduct By Former Management

1. Decisions with respect to the privilege properly lie with the trustee. This result serves the important policy of preventing officers and directors from abusing the corporation's privilege to shield their own wrongdoing and prevent the effective assertion of valid claims by those injured by their actions. The trustee is a fiduciary independent of prior management.[46] In addition to operating the debtor's busi-

[45] Because of the volatility of commodity futures markets, even in normal circumstances the financial condition of a firm can change dramatically from week to week and thus account statements and other records may not accurately reflect the condition of the firm or its accounts. See 46 Fed. Reg. 62864 (1981).

[46] Directors and officers are "insiders" who may not vote in the election of the trustee (11 U.S.C. 101(25)(B)(i) and (ii), 702(a)(3)).

ness, the trustee must, in seeking to maximize the value of the estate, investigate the conduct of prior management to uncover and assert causes of action against the debtor's officers and directors. Especially where a bankruptcy is precipitated by insider misconduct, such causes of action are important assets of the estate. See generally 11 U.S.C. 704(4), 547, 548. Fulfillment of the trustee's duty to discover these causes of action would often be impossible if former management were allowed to control the corporation's attorney-client privilege.[47] See generally *In re Browy*, 527 F.2d 799, 802 (7th Cir. 1976); Securities and Exchange Commission Report on the Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees, Pt. VIII, 109-110 (1938) (SEC Report) (management, because of a conflict of interest, frequently impedes the estate's recovery of assets that management has wrongfully diverted or appropriated).

[47] The court of appeals' decision may go as far as casting doubt on the trustee's ability to obtain information during the course of the trustee's own examination of the debtor corporation's counsel: the claim of privilege has been asserted here against the trustee as well as the Commission. See Trustee's Pet. Amicus Br. 3-4 (examination of Weintraub was undertaken by trustee as well as by the CFTC). See generally, *e.g.*, 11 U.S.C. 542(e) (disclosure of recorded information to trustee is "[s]ubject to any applicable privilege"); *In re O.P.M. Leasing Services, Inc., supra*; *In re Silvio De Lindegg Ocean Developments, Inc., supra*; *In re Vantage Petroleum Corp., supra.* Whatever the arguments with respect to whether it is appropriate in particular circumstances for the trustee to waive the privilege and thus authorize (or make) disclosures to third parties (see pages 34-36 & note 63, *infra*), there is no justification for using the corporation's privilege to withhold information from the trustee himself.

In this very case, respondent Frank McGhee was convicted in 1983 of embezzling $3.5 million in CDCB's customer funds, in violation of Section 9(a) of the Commodity Exchange Act, 7 U.S.C. 13(a), and was sentenced to three years' incarceration. *United States* v. *Frank McGhee*, No. 83 CR 262-1 (N.D. Ill. Oct. 7, 1983). Further, both respondents have actual or potential personal liability to the CDCB estate exceeding $4 million. Trustee's Pet. Amicus Br. 8. Respondents consequently have an obvious conflict of interest with respect to whether the corporation's attorney-client privilege should be exercised.[48] Cf. *Pepper* v. *Litton*, 308 U.S. 295, 306 (1939).[49] Allowing the very insiders who may have defrauded the corporation to veto the trustee's waiver of the privilege would prejudice the interests of the debtor and its creditors and customers, and would defeat the privilege's purpose of "promot[ing] broader public interests in the observance of law and administration of justice" (*Upjohn Co.* v. *United States*, 449 U.S. 383, 389 (1981)). Officers and directors who no longer manage the corporation cannot

[48] Accordingly, even if the trustee would not otherwise have the power to waive the privilege, he should be able to do so where the sole objecting parties have such a conflict. Cf. *Garner* v. *Wolfinbarger, supra* (shareholders may for good cause overcome management's assertion of attorney-client privilege in derivative action).

[49] See also, *e.g.*, *In re O.P.M. Leasing Services*, 13 Bankr. 54, 62 (Bankr. S.D.N.Y. 1981); *In re O.P.M. Leasing Services*, 13 Bankr. 64, 70 (S.D.N.Y. 1981) (in view of the apparent conflict of interest on the part of individuals attempting to assert the debtor corporation's attorney-client privilege, even if they have some claim to speak for the corporation they may not assert its privilege to protect their personal interests).

be expected to act in its best interests: the only motive they might have for asserting the corporate privilege would be the protection of their own personal interests. See generally *Valente* v. *Pepsico, Inc.*, 68 F.R.D. 361, 369-370 n.16 (D. Del. 1975).

On the other hand, the policy concerns expressed by the court of appeals (Pet. App. 9a-11a) are misplaced.[50] The "potential chilling effect on attorney-client communications" (*id.* at 10a) is no greater here than in the case of a solvent corporation: individual officers and directors always run the risk that present or successor management may waive the corporation's privilege with respect to their communications with counsel (see pages 10-11, *supra*).[51] No in-

[50] The court's concerns are especially unpersuasive because it failed to take into account that the attorney-client privilege, which inhibits the truth-seeking process, must be "strictly confined within the narrowest possible limits consistent with the logic of its principle." 8 *Wigmore on Evidence, supra*, § 2291, at 554. See *Trammel* v. *United States*, 445 U.S. at 50.

[51] *In re O.P.M. Leasing Services*, 13 Bankr. at 57, 67-68. Individual officers' interests and those of the corporation may coincide; but management may determine that the officer acted in his own self-interest to the detriment of the corporation. Cf. *New York Central & Hudson River R.R.* v. *United States*, 212 U.S. 481, 492-495 (1909); Note, *Corporate Crime: Regulating Corporate Behavior Through Criminal Sanctions*, 92 Harv. L. Rev. 1227, 1246-1252 (1979). In that situation, management acting as a collective entity has a strong interest in waiving the privilege. And even if the corporation may face some potential liability for its officers' or employees' misconduct, the corporation may determine that it is in its best interest to attempt to avoid liability by promptly bringing the misconduct to the attention of government authorities. See Fauretto & Reeves, "Department of Justice Disclosure" in Block & Pickholz, *The Internal Corporate Investigation* 253-265; Mann, "Disclosure of Results of Investigation," *supra*, at

dividual has the legitimate expectation that the corporation will later assert the privilege for his personal benefit.[52] The chilling effect, if any, arises in all such cases from the fact that the privilege is that of the corporation, not its officers or directors.

The court's statement (Pet. App. 9a) that waiver by the trustee would "condone an inequality of treatment between bankrupt corporations and bankrupt individuals" is also unpersuasive. Corporations, as "artificial creature[s] of the law" (*Upjohn Co.* v. *United States*, 449 U.S. at 389-390), must act through natural persons to exercise their rights. It does not discriminate against a corporation to designate the trustee—who now constitutes the "management"—as the person to act on its behalf.[53] Finally,

117-125. In any event, reporting requirements imposed on public corporations may require disclosure of misconduct on the part of management. See *Handler* v. *SEC*, 610 F.2d 656 (9th Cir. 1979); *SEC* v. *Joseph Schlitz Brewing Co.*, 452 F. Supp. 824 (E.D. Wis. 1978); Block & Barton, *Internal Corporate Investigations: Maintaining the Confidentiality of a Corporate Client's Communications with Investigative Counsel*, 35 Bus. Law. 5 (1979).

[52] In internal investigations of possible wrongdoing, corporate counsel routinely advise corporate officers and employees that the attorney represents the corporation and that the individual may not be able to assert a privilege with respect to his communications to the attorney. See Kirkpatrick, "How to Conduct An Internal Corporate Investigation," in Block & Pickholz, *supra*, at 82; Bialkin, "Legal and Practical Considerations for Disclosure of the Results of an Internal Corporate Investigation," *supra*, at 145.

[53] The court's statement (Pet. App. 10a) that waiver by the trustee would allow the attorney-client privilege to "vanish" on the "whim" of the trustee is plainly incorrect. The trustee's waiver must be based on his judgment as to the best

the court's concern (Pet. App. 10a) over discrimination against bankrupt corporations as compared to solvent ones is groundless. The same rule applies to both: the privilege may be waived by the present management. Any difference in treatment results from the fact that the management of a corporation undergoing liquidation is placed in the hands of a trustee pursuant to the Bankruptcy Code.[54] Indeed, the court of appeals' decision works to the disadvantage of corporations in bankruptcy by preventing them from effectively pursuing valid claims against officers and directors. Cf. *Handler* v. *SEC*, 610 F.2d 656 (9th Cir. 1979).

2. Denying the trustee authority over the debtor's attorney-client privilege would foreclose an important avenue of voluntary cooperation between the government and bankruptcy trustees. Such a result would

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interests of the estate (see pages 34-36, *infra*), not on a "whim." Cf. *In re Curlew Valley Associates*, 5 Collier Bankr. Cas. 2d 255, 259 n.5, 264 (Bankr. D. Utah 1981) (business judgment rule applies to decisions of reorganization trustee). And waiver of the privilege by the trustee, acting for the debtor, no more causes the privilege to "vanish" than does any other proper waiver by the party authorized to make it.

[54] Of course the Bankruptcy Code is premised on the need to treat insolvent individuals and corporations differently from solvent ones. See generally, *e.g.*, *NLRB* v. *Bildisco & Bildisco*, *supra*. The Code provides debtors with certain important advantages, such as a stay of creditors' actions (11 U.S.C. 362). See also SEC Report, 107 ("When a corporation avails itself of the protection of the bankruptcy court, it is enabled to stave off its creditors. The court protects its property from dismemberment by executions and attachments. It has the benefit of what in equity was of the 'chancellor's umbrella'. But that umbrella should not be held by the debtor, but by the court through its trustee.") (citations omitted).

prevent the trustee from conducting effective investigations into causes of action against former management at the least cost to the estate as well as seriously impede the government's ability to enforce criminal, commodity and securities laws.

Corporate bankruptcies are not infrequently associated with fraud or other misconduct by former management.[55] When corporate management outside bankruptcy initiates an investigation of individual officers and directors who are suspected of misconduct—an increasingly common occurrence[56]—it is not acting contrary to the *corporation's* self-interest.[57] The trustee in bankruptcy is acting no differently. In either case, the investigation is conducted to protect the property and economic interests of the entity.[58]

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[55] Such misconduct may have particularly severe repercussions with respect to the bankruptcy of commodity brokers. See pages 19-21, *supra*. The Commission's effectiveness in this area is therefore especially important. Accordingly, the CFTC has the right to appear and be heard on any issue in commodity broker liquidations (11 U.S.C. 762(b)), and qualifies as a party in interest. As such, the Commission has participated in the CDCB liquidation. Similarly, insider misconduct often results in the bankruptcy of publicly held corporations. See, *e.g.*, *In re Equity Funding Corp.*, 375 F. Supp. 1378, 1380-1381 (J.P.M.D.L. 1974); *In re Saxon Industries, Inc.*, 29 Bankr. 319 (Bankr. S.D.N.Y. 1983). In part because of the frequency of such occurrences, the SEC has the right to participate in reorganization proceedings under Chapter 11 (11 U.S.C. 1109(a)). See S. Rep. 2073, 75th Cong., 3d Sess. 6-10 (1938).

[56] See Mann, "Disclosure of Results of Investigation," in Block & Pickholz, *supra*, at 109.

[57] See, *e.g.*, *id.* at 116; note 51, *supra*.

[58] Waiver of a corporation's attorney-client privilege in order to advance its economic interests is consistent with the

Management often will conclude that voluntary cooperation with the government in its investigations of prior management, including, when appropriate, waiver of the attorney-client privilege, is in the best interests of the corporation.[59] The trustee may likewise determine that it is in the estate's best

nature of the privilege itself as it applies in the corporate context. The purpose of the privilege is, of course, to encourage full and frank communications between attorneys and their clients. *Upjohn Co.* v. *United States,* 449 U.S. 383, 389 (1981). Such communications on the part of corporate agents to corporate counsel are valued as a means of asserting and defending the corporation's economic interests and property rights. *In re Silvio De Lindegg Ocean Dev., Inc.,* 27 Bankr. at 28; see also *Joy* v. *North,* 692 F.2d at 887 (decision to bring a lawsuit is a "corporate economic decision"); cf. *Bellis* v. *United States,* 417 U.S. 85, 89-92 (1974); *United States* v. *White,* 322 U.S. 694, 699-700 (1944); see generally, *e.g., Hooper* v. *Mountain States Securities Corp.,* 282 F.2d 195, 206-207 (5th Cir. 1960), cert. denied, 365 U.S. 814 (1961) (fraud on corporation is as an injury to property); *Empire Tractor Corp.* v. *Time, Inc.,* 91 F. Supp. 311, 312 (E.D. Pa. 1950) (libel action on behalf of corporate plaintiff "is concerned exclusively with an injury to property" and so may be pursued by bankruptcy trustee). Hence, access to and control over the communications on the part of the trustee to advance the economic interests of the estate will not impede any interest legitimately served by the communications themselves. If the attorney is also acting as counsel for an individual corporate agent, that agent may be able to assert the privilege in his own right. *E.g., Diversified Industries, Inc.* v. *Meredith,* 572 F.2d 596, 611 n.5 (8th Cir. 1978) (en banc); *Citibank,* 666 F.2d at 1196.

[59] See Herlihy & Levine, *Corporate Crisis: The Overseas Payment Problem,* 8 Law & Policy in Int'l Bus. 547 (1976). In and out of the bankruptcy context, voluntary cooperation by persons or corporations being investigated by the government is important to the effective enforcement of the law.

interest to allow the government to undertake the burden and expense of such investigations, and then to file civil actions in their wake.[60] Such an approach conserves the estate's limited assets and may provide the best opportunity for discovery of significant causes of action on behalf of the estate.

In seeking control over privileged information, the trustee is not acting as a prosecutor in conflict with the corporation.[61] To the contrary, his disclosure of the information may be necessary in order to maximize the assets of the estate.[62] The trustee acts not merely for creditors, but for all claimants to the estate, including the corporation's equity holders. See

[60] The Commodity Exchange Act contemplates that the Commission will provide such assistance to trustees. In a 1982 amendment to Section 8(a) of the Act (7 U.S.C. 12(a)), Congress authorized the Commission to disclose confidential market and business information to equity receivers and bankruptcy trustees for commodity brokers to assist them in their efforts to marshal assets for distribution to customers. See *CFTC Reauthorization: Hearings on H.R. 5447 Before the Subcomm. on Conservation Credit and Rural Development of the House Comm. on Agriculture,* 97th Cong., 2d Sess. 11 (1982) (statement of Philip McBride Johnson, Chairman, Commodity Futures Trading Commission); *CFTC Reauthorization: Hearings on S. 2109 Before the Subcomm. on Agricultural Research and General Legislation of the Senate Comm. on Agriculture, Nutrition, and Forestry,* 97th Cong., 2d Sess. 5 (1982) (statement of Philip McBride Johnson).

[61] Such a mischaracterization underlies the decision in *In re Vantage Petroleum Corp.,* 40 Bankr. at 40, which followed the decision of the court of appeals in this case.

[62] Indeed, the trustee often requires control over privileged information to raise defenses to claims against the estate's property. See 11 U.S.C. 541(e) (redesignated by Pub. L. No. 98-353, §§ 456(d), 470, as 11 U.S.C. 558 (1984)); cf. *Miller* v. *New York Produce Exchange,* 550 F.2d 762, 767-768 (2d Cir.), cert. denied, 434 U.S. 823 (1977).

pages 16-17, *supra*. His function in waiving the attorney-client privilege is not to enable him to attack former management, but simply to increase the assets of the estate.[63]

The principal application of the decision below will be to situations where prior management has, through illegal actions, injured the corporation and its creditors, shareholders, and customers. It grants officers and directors of insolvent corporations the power to foreclose effective investigation into their own misconduct, and will thereby frustrate the legitimate efforts of bankruptcy trustees and law enforcement authorities.

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[63] Where it is not, in the trustee's judgment, in the best interests of the estate because of possible third-party claims, the trustee presumably would not waive the privilege. See Chicago Note 22. This case relates solely to the trustee's power over the privilege. It does not raise the issue whether the waiver here was in the best interests of the estate, which is a question to be determined in the first instance by the bankruptcy court. Respondents, however, did not challenge the trustee's waiver in bankruptcy court and they may not do so for the first time here as a defense to this subpoena enforcement action. In any event, the waiver here plainly would be beneficial to the estate, as it would enable the trustee to obtain the assistance of the Commission in uncovering assets of the estate. There has been no suggestion of possible losses *to the estate* that might outweigh these gains.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

REX E. LEE
Solicitor General

PAUL M. BATOR
Deputy Solicitor General

BRUCE N. KUHLIK
Assistant to the Solicitor General

KENNETH M. RAISLER
General Counsel

WHITNEY ADAMS
Deputy General Counsel

HELEN G. BLECHMAN
Attorney
Commodity Futures Trading Commission

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